STATE OF CALIFORNIA
DEPARTMENT OF INSURANCE
45 Fremont Street
San Francisco, CA 94105

RH03029826 **June 2, 2006**

Title 10
Proposed Revisions to Sections 2632.5, 2632.8 and 2632.11
Optional Automobile Insurance Rating Factors

Summary and Response to Volume 12 Comments Received During 45-day Comment Period

Responses to Common Comments:

1.1: Common Comments:

- Rates should be cost-based / substantially related to the risk of loss
- A driver's location (zip code) should be a critical factor in calculating insurance rates
- Drivers in rural regions of the state should not be forced to subsidize the rates for drivers in urban regions of the state.
- The proposed regulations will result in arbitrary rates because of the act of pumping and tempering, the resulting cross-subsidies, etc.

Response:
The Commissioner's regulations continue to permit a driver's location to be an important factor in setting insurance rates. While the proposed regulations preserve the importance of location in setting insurance rates, however, Proposition 103 provides that the factors which determine a driver's rates should be weighted in a specific order of importance. The proposed regulations will implement the weight ordering requirement of Proposition 103, which is codified in Insurance Code section 1861.02(a). The ballot pamphlet to Proposition 103 promised, in part, that "103 forces insurance companies to base your rates on your driving record first, rather than on where you live. That means good drivers throughout the state will pay less than they do now, while bad drivers will pay more." The ballot pamphlet also establishes that "In general, the measure requires that rates and premiums for automobile insurance be determined on the basis of the insured person's driving record, miles driven and number of years of driving experience." Finally, in the clearest possible terms, section 1 of Proposition 103 declares under the heading "Findings and Declaration" that "automobile insurance rates shall be determined primarily by a driver's safety record and mileage driven." To the extent that the cost of insurance may increase for some low income drivers and may affect businesses in rural or urban parts of the state, the increase will be determined primarily by the driver's safety record, mileage driven and years of driving experience, as Proposition 103 intended.

While some commentators believe that territory is the most important characteristic for determining the likelihood of an accident, there are other equally important, if not more important considerations which insurers often neglect under the existing regulations. Driving safety record, for example, is a very strong predictor of the risk of loss for an accident. Similarly, annual mileage driven bears a strong correlation to the risk of loss for an accident. The Department commonly observes instances where insurers do not collect meaningful data regarding the correlation between some of the mandatory factors and the risk of loss. One rating factor where insurer data is lacking is the mandatory factor of annual mileage driven. By way of example, the Commissioner has observed that one insurer arbitrarily places insurers into one of merely two categories: drivers that drive less than 7,500 miles per year and drivers who drive more than 7,500 drivers per year. Other examples show similar neglect for data collection regarding the mandatory factors. The existing regulations do not encourage insurers to develop better data collection for the mandatory rating factors, because they allow insurers to fall back on the crutch of territory for auto rating. The proposed regulations will stimulate insurers to conduct better data collection for mileage and driving safety record. This, in turn, will enhance the relationship to the risk of loss between those rating factors and the rates developed under the proposed regulations.

This comment contends that unlike the existing regulations, the proposed regulations will not be cost based and/or substantially related to the risk of loss.

The Court in *Spanish Speaking Citizens' Foundation v. Low* concluded that the language in Insurance Code section 1861.02(a)(4) which requires optional factors to be "substantially related to the risk of loss" also requires that the mandatory factors, and their order of importance must be substantially related to the risk of loss. The Commissioner notes, however, that Insurance Code section 1861.02(a)(4) expressly makes reference to the optional factors alone. Indeed, the Commissioner believes that Proposition 103 sought to bring fairness to automobile insurance rates, in part, by requiring the mandatory factors of driving safety record, annual miles driven and years of driving experience to assume greater weight than the optional factors irrespective of the mandatory factors' relationship to the risk of loss. While the Commissioner disagrees with the Court's interpretation of Insurance Code section 1861.02(a)(4) and the meaning of "substantially related to the risk of loss", the Commissioner recognizes that the *Spanish Speaking* decision represents the current state of the law, and his response takes into account the Court's interpretation in *Spanish Speaking.*

Notwithstanding the Commissioner's interpretation of Insurance Code section 1861.02(a)(4), the *Spanish Speaking* Court determined that for purposes of the weight ordering mandate, "interpretations that preserve a substantial relationship between premiums and the risk of loss … are [] to be favored over those that would produce arbitrary rates." (*Spanish Speaking Citizens' Foundation v.* Low (2000) 85 Cal.App.4th 1179, 1227.) The commentator contends that the existing regulations are substantially related to the risk of loss, but that the proposed regulations are not and therefore are invalid. The fundamental assumption here is that the present rate regulations ensure cost-based rating. This assumption is demonstrably incorrect.

First, Proposition 103 as well as other laws reflect the voters' and Legislature's intent that public policy objectives must often prevail over considerations of cost-based pricing. For example, many insurers contend that a policyholder's lack of a history of prior insurance bears a strong correlation to the risk of an automobile accident. Despite insurers' preference for using the absence of prior insurance as a rating factor, Insurance Code section 1861.02(c) prohibits its use. (See, e.g., *Foundation for Taxpayer and Consumer Rights*, *et al. v. Garamendi* (2005) 132 Cal. App. 4th 1354.) Other examples of laws which require public policy to take precedence over an argument of cost-based pricing abound. (See, e.g. Ins. Code section 11628 & 679.71 [sex, race, color, religion, national origin, or ancestry cannot by itself constitute a risk for which a higher rate may be charged].) Directly at issue, Insurance Code section 1861.02 requires that automobile rates be determined by applying "in decreasing order of importance" the mandatory factors of driving safety record, annual mileage driven and years of driving experience, followed by any optional factors adopted by the Commissioner. Thus, concerns about cost-based pricing and the relationship to risk of loss often must yield to greater concerns of public policy, as reflected in the weight ordering requirements mandated by section 1861.02(a).

Moreover, the Department has observed numerous examples of rates which are not cost-based under the existing regulations, both within the course of this rulemaking proceeding as well as during its review of rate filings submitted to the Department. The Department's Rate Filing Branch commonly receives rate filings from insurers under the current regulatory system in which the insurers select rate assignments that do not reflect the cost of providing the insurance. For example, although an insurer's loss experience might require an indicated rate relativity for a particular zip code for a cost-based rate, insurers commonly select different rate relativities which markedly deviate from the indicated rate relativity.

While the existing regulations do not result in rates that are purely cost-based, the Court in Spanish Speaking Citizens concluded that regulations which "preserve a substantial relationship between premiums and the risk of loss … [are] to be favored over those that would produce arbitrary rates." (*Spanish Speaking Citizens' Foundation v. Low* (2000) 85 Cal.App.4th 1179, 1227.) The proposed regulations, like the existing regulations, do not reflect rates which are in lockstep with a given insurer's loss experience. This situation exists not only because Proposition 103 dictates that some public policy objectives must often override the relationship to the risk of loss, but also because insurers often prefer to select rates which are different from the insurer's loss experience. Nevertheless, the proposed regulations, like the existing regulations, do preserve a substantial relationship between premiums and the risk of loss, and therefore cannot be considered arbitrary or contrary to Insurance Code sections 1861.02(a) and 1861.05.

Similarly, some commentators contend that rating factors which are enhanced or diminished (i.e. – "pumped" or "tempered") to bring the factors into the appropriate weight order are not cost-based and therefore not substantially related to the risk of loss. Under the existing regulations, however, the Department has observed instances of rate

filings in which insurers "pump" the mandatory factor of years driving experience, so that they can increase the influence of zip code on an insured's rate. Indeed, State Farm's comments regarding this rulemaking proceeding recognize that the existing regulations could require pumping or tempering in some cases. Just as the Department recognizes that public policy objectives may take precedence over cost-based rating, the Department recognizes that rates can still be substantially related to the risk of loss despite the fact that some rating factors are pumped or tempered as necessary to bring the rating factors into the correct weight order required by Insurance Code section 1861.02.

Because the proposed regulations ensure that zip code (territory) may be as high as the fourth-most important factor in calculating an insured's premium, rates will still be substantially related to the loss costs associated with a particular region of the state. The Commissioner's proposed regulations achieve the most appropriate balance among the objectives of Proposition 103. Unlike the existing regulations, the proposed regulations ensure that rates will be determined primarily by driving safety record and mileage driven, while still permitting other optional rating factors with a substantial relationship to the risk of loss to have a significant influence on premiums.

1.2: Common Comments:

- The existing regulations produce lower premiums for more good drivers than other alternatives.
- The proposed regulations will raise rates for good drivers in rural regions of the state.
- The proposed regulations will raise rates for low income drivers in rural regions of the state.

Response:

While the Court of Appeal in *Spanish Speaking Citizens v. Low* concluded that the current regulations are lawful, the Court also acknowledged that a method identical to the Commissioner's proposed regulations may also represent a permissible interpretation of Proposition 103. To the extent that the commentator suggests that the current regulatory system produces lower premiums for more good drivers, the Commissioner disagrees, as he has observed substantial evidence to the contrary. Indeed, because the proposed regulations ensure that how you drive will be more important than where you live, it is axiomatic that more good drivers will experience rate decreases under the proposed regulations than under the current regulatory system.

1.3 Common Comments:

- The proposed regulations should be fair for all regions of the state and not just urban regions of the state.
- The Commissioner's proposed regulations ignore the impact upon rural and suburban regions of the state.

Response:

The Commissioner has considered the impact upon both rural and urban drivers in the state. After receiving a petition for rulemaking in May of 2003, the Commissioner personally attended seven informational meetings in regions of the state ranging from Fresno and Chico to Los Angeles and Oakland to discuss the potential impact of the proposed regulations upon rates for urban and rural regions of the state. The Commissioner observed numerous instances – in rural as well as urban locations – where drivers with identical characteristics would pay unjustifiably different premiums simply because they live in the "wrong" zip code.

For example, the Commissioner has observed substantial variations in premium not only for consumers living within just a few miles of each other, but even for neighbors who live in adjoining zip codes. In fact, the differentials in territory relativities between adjacent zip code pairs for some companies do not closely follow the patters of the industrywide pure premium data. In looking for examples of arbitrary rates and premiums, one need look no further than the premiums established under the existing regulations. Examples such as these demonstrate that the existing regulations are neither purely cost-based nor consistent with Proposition 103's distaste for zip code rating. The Commissioner's proposed regulations will prevent similar disparity between zip codes in the future, by requiring insurers to give more consideration to how you drive rather than where you live. Not only does this approach make sense, it is the approach that the Proposition 103 ballot pamphlet promised to the voters.

1.4 Common Comments:

- According to studies performed by Robert Downer and Mercer Actuarial Consulting, Inc., the proposed regulations will result in an XX% increase for XX drivers. Rates will increase for 52 out of 58 counties.

Response:

At the outset, it is important to point out that any projection of premium that a particular consumer or even a particular region of the state may pay due to the proposed regulations is a matter of substantial speculation. The Commissioner's proposed regulations provide a significant degree of discretion to insurers to decide upon the most prudent manner for implementing the proposed regulations. This discretion exists, in part, because the proposed regulations permit insurers to use any combination of pumping or tempering of rating factors necessary to achieve the order of importance required by section 1861.02(a). Because different insurers will use different rating factors and different methods for achieving compliance with the proposed regulations, it would be virtually impossible to perform a study which would show the precise effect that the proposed regulations will have upon premiums for Californians statewide. Generally speaking, the Commissioner's proposed regulations grant an insurer broad discretion to implement the proposed regulations, so long as a given insurer's rates assign the greatest weight to 1) driving safety record, followed by 2) annual miles driven, followed by 3) years of driving experience, followed by 4) any optional rating factors, weighted individually. While some studies have projected an average rate change for a particular region of the state, the impact of such projection upon a particular consumer will vary significantly due to the unique characteristics of each consumer. Additionally, to date, no study has explored all

of the possible methods by which any given insurer may choose to comply with the proposed regulations. For each of these reasons and others, any comment which suggests that premiums will raise or lower for a particular region of the state by an average of X% is purely speculative and fails to ignore the unique nature of each driver's characteristics as well as the unique manner in which each insurer will choose to comply with the regulations.

This comment includes a figure that suggests a particular County's drivers will receive rate increases of a particular size due to the Commissioner's regulations. To the extent that this comment is referring to the Mercer Actuarial Consulting, Inc. study, the figure appears to have been derived from "Instruction set 3" which was designed to replicate the results of a study performed by Robert Downer. As explained below, the Downer study does not represent an accurate portrayal of the impact of the proposed regulations on Californians' auto rates. Instruction sets 1 and 2, by comparison, showed substantially different and more favorable premium changes for good drivers in all regions of the state.

To the extent that this figure comes from a study produced by Robert Downer, it is important to note that the Downer study produced substantially flawed results which do not represent a reasonable projection of the way in which insurers will comply with the proposed regulations. The Downer study chose to diminish the effect of (i.e. – "temper) any optional factor that was greater than the factor of years of driving experience. At the same time, the Downer study did not permit the possibility of increasing the effect of (i.e. – "pumping") other factors, or a combination of diminishing some factors and increasing others. The proposed regulations, like the existing regulations, permit any insurer to pump or temper any rating factor as necessary in order to achieve compliance. This procedure was not implemented by Mr. Downer's study and directly resulted in the substantial premium shifting projected by Mr. Downer. The Downer study, in short, does not accurately reflect the manner in which insurers will implement the proposed regulations. Because the findings in the Downer study do not accurately reflect the manner in which insurers may implement the proposed regulations, they are irrelevant and consequently have been rejected by the Commissioner.

Mr. Downer's comments regarding the proposed regulations include a new study which he apparently performed in February of 2006. For the reasons described above, this study, like the Mercer data and Mr. Downer's previous study, are constrained by the same limitations and to a reasonable degree of certainty will not reflect the methods of pumping and tempering that individual insurers will use to comply with the proposed regulations.

1.5 Common Comments:

- **Seniors living in rural regions of the state should not be penalized by the proposed regulations.**

Response:
Proposition 103 provides that the number of years of driving experience must be the third most important rating factor, in terms of the weight given to each rating factor. Because

different insurers use differing characteristics to rate drivers according to their age and driving experience, whether a given consumer's age will result in a higher or lower auto insurance rate under the proposed regulations will largely depend upon which insurance company the consumer selects for coverage. Consumers who compare prices before purchasing automobile insurance may find that they will qualify for a lower insurance rate.

1.6 Common Comments:

- **The Downer Study and Instruction Set #3 from the Mercer Study suggest rates in my county will increase by X%.**

Response:

As with many of the figures cited in similar comments submitted to the Department, the figures cited in this comment do not bear a reasonable relationship to the likely rate impact of the proposed regulations. The percentage increase in rates described by this commenter appears to be based upon the results of the Downer study and the related results of Instruction set 3 from the Mercer Study. As explained in Response 1.4 above, the Downer study produced substantially flawed results, because Mr. Downer's analysis simply tempered the weight of the optional rating factors, without allowing for the pumping of mandatory factors. In other words, Mr. Downer's analysis sought to place the burden of the entire shift in a consumer's rate on territory without adjusting other rating factors to affect the rate. The Commissioner's regulations, however, do not condone such an approach. In fact, the Commissioner's regulations envision that insurers will do more than merely temper those factors, such as territory, which are weighted too heavily under Proposition 103. The Commissioner's regulations also seek to force insurers to pump, i.e. - give greater consideration to factors such as years licensed, annual mileage driven and driving safety record – factors that insurers have traditionally placed less emphasis on, when compared to the emphasis placed upon territory.

1.7 Common Comments:

- **The proposed regulations will produce rates which are not actuarially sound.**
- **The proposed regulations, by creating cross-subsidies, violate actuarial standards of practice.**
- **The proposed regulations are unfairly discriminatory or are not substantially related to the risk of loss because they are not actuarially sound.**

Response: As compared to the existing regulations, the Commissioner's proposed regulations represent the lawful interpretation of Proposition 103. Insurance Code section 1861.02 requires that every optional factor, such as territory, be given less weight than driving safety record, annual miles driven or years of driving experience. The American Academy of Actuaries' Statement of Principles for Risk Classification provides that actuarial standards must yield to social acceptability guidelines, including applicable law. (American Academy of Actuaries, Risk Classification Statement of Principles, p. 14, para. H.) Because optional factors must be given less weight than under the proposed

regulations in order to ensure that the mandatory factors are most important as section 1861.02 requires, the resulting rate cannot be considered actuarially unsound on this basis. Moreover, the Commissioner has observed substantial evidence to suggest that rates under the current regulatory system are often not tied to the risk of loss. Indeed, whether territory, gender, marital status or a multiple car discount are entitled to the significant weight they are given by many insurers under the existing regulations is a subject of considerable disagreement within the insurance ratemaking community.

1.8 Common Comments:

- **The proposed regulations violate *Spanish Speaking Citizens' Foundation v. Low*, because they allow for pumping and tempering.**
- **The proposed regulations violate *Spanish Speaking Citizens' Foundation v. Low*, because they create rates which are not based on the cost of providing insurance.**
- **The proposed regulations violate *Spanish Speaking Citizens' Foundation v. Low*, because rates which are not cost-based are arbitrary.**

Response: Although the Court in *Spanish Speaking Citizens* considered the standards of Proposition 103 and concluded that rates which deviated from cost-based pricing would violate Proposition 103's prohibition against arbitrary rates, the Court also conceded that "there may be no one single correct interpretation" of Proposition 103's competing requirements. (*Spanish Speaking Citizens' Foundation v. Low* 85 Cal.App.4th 1179, 1231.) The Court also acknowledged that the existing regulations do not ensure that rates will be determined primarily by driving safety record and mileage driven, as the ballot pamphlet to Proposition 103 intended. (*Spanish Speaking Citizens* 85 Cal.App.4th at 1237-38.) Recognizing the competing goals of Proposition 103, and the fact that rates are not determined primarily by driving safety record and mileage driven, the Court noted that an interpretation of Proposition 103 identical to the interpretation set forth in the Commissioner's proposed regulations, "may be a permissible interpretation of [section 1861.02]." (*Spanish Speaking Citizens* 85 Cal.App.4th at 1239.)

1.9 Common Comments:

- **The proposed regulations do not account for the likelihood of theft in urban areas versus rural areas**
- **The proposed regulations do not account for the likelihood of vandalism claims in urban areas versus rural areas.**

Response:
Claims for vehicle theft or vandalism generally fall under an insurance policy's comprehensive coverage. Claims under that coverage may have limited correlation to the mandatory rating factors. To the extent that comprehensive coverage bears less of a relationship to the mandatory factors of driving safety record, mileage driven and years of driving experience, the Commissioner has revised the regulations to account for the unique concerns raised by comprehensive coverage. Title 10 California Code of Regulations section 2632.8(a) permits an insurer to combine comprehensive coverage

with collision coverage to enhance the proposed regulations' substantial relationship to the risk of loss. The regulatory change which will allow such combination will comply with Proposition 103's weight ordering requirements insofar as comprehensive coverage and collision coverage represent a policy "combination thereof" as described in section 660(a).

Volume 12, Tab No. 5:

Commentator: Robert Bernstein
Date of Comment: March 5, 2006
Type of Comment: Written

Summary of Comment (page 1, paras.1&2): Insurers should be required to maintain a minimum number of categories to accurately measure the increased loss costs associated with a particular rating factor. Insurers should also be required to collect accurate data in order to avoid forcing other drivers to pay more than is necessary. Insurers do not accurately measure higher mileage, for example.

Response to Comment: While the Commissioner agrees with the commentator that many insurers do not use sufficient categories to accurately measure the loss costs for particular rating factors, some would argue that any effort by the Commissioner to dictate the minimum number of relativities that an insurer must use would be unduly burdensome. One of the goals of Proposition 103 was to encourage competition. To this end, the Commissioner intends to preserve the flexibility for insurers to design class plans in the manner they choose, so long as the class plans comply with applicable law. Rather than require insurers to maintain a minimum number of categories, the proposed regulations will require insurers to give more importance to the mandatory rating factors of driving safety record, annual mileage driven and years of driving experience. The Commissioner anticipates that these regulations will create a natural incentive to encourage insurers to use better and more accurate methods to measure rating factors such as annual mileage. Thus, the proposed regulations will still give insurers the flexibility to decide upon the most appropriate method for measuring loss costs for each factor, but will also ensure that the mandatory factors have the greatest influence on an insured's rate.

Summary of Comment (page 1, para.3):
Insurers should be permitted to use a pre defined set of insureds to measure the weights of their rating plan. Although the Department currently allows this, the pre-defined set used by the Department is outdated and is too large.

Response to Comment: While the Commissioner is interested in considering further enhancements to his existing alternative weighting files, the commentator's proposal is beyond the scope of this rulemaking proceeding.

Summary of Comment (page 1, para.4):

The court will not uphold the proposed regulations unless the Department places a maximum, like 10%, for pumping or tempering the rating factors. If you allow insurers to pump or temper by more than 10%, you cannot claim to produce rates which are close to cost-based rating.

Response to Comment: Placing a limitation upon the amount by which an insurer may pump or temper may not ensure that driving safety record, annual miles driven and years of driving experience will be the most important rating factors for determining an automobile insurance rate. Therefore, the commentator's suggestion would place Proposition 103's weight ordering requirement in jeopardy. The Commissioner expects that the placement of caps on pumping and tempering will create unnecessary work for an insurer when complying with the proposed regulations. Moreover, the Commissioner is confident that rates under the proposed regulations will not need caps on pumping and tempering in order to remain substantially related to the risk of loss for the reasons stated in response to Common Comment 1.1.

Summary of Comment (page 2, para.5):

The phase-in period for the proposed regulations should limit pumping and tempering to a maximum of 5% for 2006 or 2007, and then create larger limits in future years through 2010 or 2011. Because the Department is not equipped to handle a large number of rate filings, the phase-in should require filings to be submitted every two years.

Response to Comment:
The Commissioner has taken similar input into account and has decided upon a reasonable schedule for implementation which will give insurers flexibility to decide upon the best approach for implementation, but will also ensure that compliance is achieved in a timely manner. Therefore, while the Commissioner believes that an implementation plan which does not finish until 2011 is too much time to implement the proposed regulations, he has revised the regulations to provide for a two-year schedule. Rather than place a maximum upon the amount that an insurer may pump or temper, the Commissioner believes a minimum threshold for implementation makes more sense. This schedule provides that insurers must bring their rates at least 15% of the way towards full compliance with the proposed regulations in the first class plan filing, but gives insurers discretion to implement the remaining 85%, so long as the implementation is completed by the two-year anniversary of the date the regulations are filed with the Secretary of State. See revisions to 10 Cal. Code of Regulations section 2632.11.

Summary of Comment (page 2, para.6):
The Department should have a few actuaries specially trained in the Department to work with insurers to assist them as they work to file class plans in compliance with the proposed regulations. The class plan filing, review and approval process should be extended to 180 days so that the Department can assist insurers as they work to comply with the proposed regulations.

Response to Comment:

The Department has considered the amount of time that will be necessary to review class plan applications as well as the amount of time insurers will need to file class plans. The proposed regulations and changes to section 2632.11 represent the Commissioner's view of the most appropriate schedule for implementation. As always, the Department's rate filing staff are thoroughly familiar with the automobile rating factors and the proposed regulations and will stand ready to assist insurers as they work to comply with the proposed regulations.

Summary of Comment (page 2-3): It seems odd that the Commissioner would seek to make massive changes to the auto rating factors regulations, which could be thrown out by the Commissioner' successor. The current method of determining the weight of a particular rating factor is the Single Omit method which was developed by the commentator. The Single Omit method was designed to work with the existing regulations but will not work properly with the proposed regulations. The Commissioner should use a new method to measure weight that works with the proposed regulations.

Response to Comment:

The Commissioner disagrees with the commentator's suggestion. The current method for measuring a rating factor's weight will work well with the proposed regulations, and is not adversely affected by the changes made to the existing regulations. The Commissioner intends to continue use of a method for measuring a rating factor's weight that is consistent with the Department's prior system of measurement.

Summary of Comment (page 3-4): No magic formula will reduce premiums for all drivers. The proposed regulations will simply redistribute costs primarily among good drivers and will not reduce good drivers' premiums. The proposed regulations will result in more insureds receiving increases in their premium, will force consumers in low cost areas to pay more while permitting drivers in high cost areas to pay less and will not benefit consumers. Eliminating territory as a rating factor is not good economics and not actuarially sound. Some insurers will be priced out of the market because surcharges based on driving record without considering territory may be substantial. The proposed regulations will be bad for competition and bad for Californians.

Response to Comment:

See Response to Common Comment 1.1
See Response to Common Comment 1.2
See Response to Common Comment 1.3
See Response to Common Comment 1.7

Summary of Comment (page 4):
One way for insurers to avoid being priced out of the market will be to use a standard data set of insureds that is published by the Department, called the "alternative weighting file." This data set, however, does not appear to be used much and appears to be out of date.

Response to Comment:
This comment is not directed at the proposed regulations and therefore likely requires no response. To the extent that the commentator suggests that the alternative weighting file is an available alternative data set which will assist insurers in complying with the proposed regulations, the data set remains available for insurers to use to set automobile rates.

Summary of Comment (Page 4):
The proposed regulations will result in increased overall insurance costs for all Californians because the proposed regulations will preclude an insurer from using rating characteristics such as territory to their full advantage. Consequently, more individuals with higher risk characteristics will purchase more coverage, and insurers will be forced to increase costs overall to pay for the higher risk policyholders. The commentator's argument is supported by Actuarial Standard of Practice No. 12.

Response to Comment:

The proposed regulations will, indeed, reflect a revenue neutral change for a given insurer. The selection of rating factors, ordering of rating factor weights and decisions regarding the relativities to be used within each rating factor do not, by themselves, alter the total amount of premium that an insurer will collect. In fact, the application of rating factors to policyholders is simply the method by which the company decides how much of the total premium collected by the insurer should be allocated to each policyholder. This is the principle of revenue neutrality. To the extent that the commentator believes that policyholders who receive reductions in their rate will seek to purchase greater coverage or vice-versa, the commentator does not rely upon any data for this statement. It appears that the commentator's suggestion is merely speculative at this point. While the Commissioner will continue to carefully observe the automobile insurance marketplace after the proposed changes take effect, he does not expect the proposed regulations to undermine the financial strength of the automobile insurance market.

For the reasons stated in Response to Common Comment 1.1, the Commissioner is confident that the proposed regulations will still be substantially related to the risk of loss, and therefore will not result in improper risk distribution for insurers. Moreover, to the extent that the commentator is arguing that the proposed regulations are contrary to actuarial principles, the Commissioner disagrees for the reasons set forth in Response to Common Comment 1.7.

Summary of Comment (Page 4-5):
The Commissioner's report, entitled "Auto Insurance in California: Differentials in Industry wide Pure Premiums and Company Territory Relativities between Adjacent ZIP Codes" supports the existing regulations. The report also demonstrates that there is little truth to the suggestion that policyholders pay dramatically different rates on opposite sides of a zip code boundary. The Commissioner should respond to these comments by

providing support for his claim that insureds with identical rating characteristics that live on opposite sides of a zip code boundary pay dramatically different rates.

Response to Comment:
The Commissioner disagrees with the commentator's characterization of the Department's study. In fact, the Department's study concluded that the differentials in territory relativities between adjacent zip code pairs for some companies do not closely follow the patters of the industry wide pure premium data. (See RH03029826 Rulemaking File Comments, Volume 7, Tab 5, page 39.) To the extent that the commentator has requested support for the conclusion that policyholders with similar characteristics pay substantially different premiums on opposite sides of a zip code boundary, please see Response to Common Comment 1.3 and RH03029826 Rulemaking File Comments, Volume 7, Tab 5, pages 26-27.

Summary of Comment (Page 5-6 & 7-8):
The proposed regulations will force many in lower-cost areas of the state to pay more for insurance, despite the fact that they earn less than persons in urban areas. The proposed regulations are not mandated by Proposition 103. The differences in loss costs between urban and rural regions of the state are due to factors such as traffic density, bad traffic controls, dangerous weather, high medical costs, litigation costs and other reasons. Actual costs do vary by ZIP code and the proposed regulations are bad policy for California because they do not account for territory's correlation to cost based pricing.

Response to Comment:

See Response to Common Comment 1.1
See Response to Common Comment 1.2
See Response to Common Comment 1.3
See Response to Common Comment 1.8

Summary of Comment (Page 7-9):

The testimony of Birny Birnbaum at the February 24 rulemaking hearing should be rejected. Despite Mr. Birnbaum's testimony to the contrary, costs can and often do vary from company to company due to rate competition and because companies base their rates on their own loss costs. Mr. Birnbaum was incorrect to state that sequential analysis does not produce cost based rates. Also, contrary to Mr. Birnbaum's statements, pumping and tempering do have an effect on cost based rates. Mr. Birnbaum may not be correct to suggest that methods of sequential analysis such as a multiple regression would account for the combined effect of rating factors. Mr. Birnbaum's suggestion that the proposed regulations will be better for seniors is not true for all companies. One commentator suggested that Connecticut's laws provide some bearing on these regulations but those laws are not relevant to the proposed regulations. Placing more importance on driving safety record and mileage will not change the driving habits of consumers. Since the large gas price increases have not reduced driving, it is doubtful that making mileage more important for insurance rates will have any effect. Therefore,

because there is no support in reality for the idea that consumers are able to control their insurance costs under the proposed regulation, the proposed regulations may prove to be a failure. The handouts that were presented by Consumers Union are deceptive and should be reviewed carefully. The Commissioner has enforcement tools to deal with concerns about insurance redlining and should not rely upon the proposed regulations to control red lining. The Department should include their definition of "cost based" in their response to these comments. If the Department believes it has any actuarial or economic support for the proposed regulations they should so indicate in their response to these comments.

Response to Comment:
The majority of the commentator's remarks are directed at other persons who testified at the rulemaking hearing. Because these comments are directed at the commentators and not at the proposed regulations or the procedures followed in proposing the regulations, it is likely that no response is required. Nevertheless, to the extent that these comments could be read to indirectly concern the proposed regulations, the Commissioner offers the following response.

While costs may vary from company to company, the Commissioner has observed substantial evidence of variations in premiums from company to company which cannot be explained by cost. See, e.g., Response to Common Comment 1.3. Indeed, as Consumer's Union correctly points out, the differentials in territory relativities between adjacent zip code pairs for some companies do not closely follow the patters of the industry wide pure premium data. (See RH03029826 Rulemaking File Comments, Volume 7, Tab 5, page 39.) As Mr. Birnbaum correctly pointed out, sequential analysis does not, on its own, produce cost based rates. Sequential analysis can produce very different results, depending upon the selections made by a given insurer. These selections are not necessarily based upon concerns about cost based pricing. For a response to the commentator's statement regarding seniors, please see Response to Common Comment 1.5. With respect to the comment regarding the state of Connecticut, the Commissioner proposes these regulations in order to fulfill Proposition 103's mandate. The proposed regulations are not in any way connected to Connecticut's laws and therefore do not require further response. While the commentator contends that consumers will not be able to control their insurance costs any better through the proposed regulations, the Commissioner disagrees. Irrespective of the Commissioner's views on this subject, Proposition 103 clearly intended to assign greater importance to rating factors within consumers' control. Insofar as the proposed regulations are designed to fulfill Proposition 103's mandate, it would not be appropriate for the Commissioner to question the merits of the voters' choices. Moreover, substantial evidence suggests that consumers do, indeed, change driving habits based upon circumstances that are within their control. Despite the commentator's suggestion, the Commissioner has observed, for example, that the increase in gasoline prices have caused consumers to drive less. Therefore, the commentator's arguments to the contrary are rejected. The Commissioner does not believe that the handouts presented by Consumer's Union are deceiving. They demonstrate the very same problems that the Commissioner observed when he held town hall meetings across the state concerning these issues. Rates

are often arbitrary and unjustifiable under the existing regulations, due in part to the substantial reliance of insurers upon territory for rating purposes. While insurance redlining is a constant concern for the Commissioner, it is not the primary reason for the proposed regulations. The primary reason, of course, is to implement Proposition 103's requirement that driving safety record, miles driven and years of driving experience must be the three most important factors for calculating an insurance rate. Finally, it would be difficult to find a definition of "cost based" that all persons could agree upon. Rates which are in lockstep with pure premium experience would tend to reflect purely cost-based rates. For the reasons described in Response to Common Comment 1.1, however, evidence strongly suggests that the existing regulations do not reflect rates which are purely cost based. Moreover, the Commissioner recognizes that cost based rates must yield to greater social objectives, as explained in Response to Common Comment 1.1.

Summary of Comment (Page 9):
Insurance companies with a less than average percentage of drivers with moving violations will have to increase surcharges for drivers with any moving violations in order to comply with the proposed regulations. This, in turn, will cause drivers with moving violations to either purchase their insurance elsewhere or drive uninsured. The insurer will, consequently, lose drivers with one or more moving violations and will have no way to comply with the regulations.

Response to Comment:

The commentator's remarks ignore the effect of competition in ratemaking. As with the existing regulations, the proposed regulations will require insurers that wish to retain market share to price their insurance rates competitively, in a manner that not only ensures that the insurer's rates are adequate to pay for claims and earn a reasonable profit, but also produces rates which consumers are willing to pay. The proposed regulations provide ample flexibility to insurers to price their rates appropriately in order to retain market share.

Summary of Comment (Page 9-10):
Table 15, which lists the adjacent ZIP code pairs, shows that many of the adjacent ZIP codes do not have a significant amount of territory that adjoins many of the pairs. Also, in several cases there are distinct differences in the characteristics of the adjacent zip codes, such as is the case with the zip code pair that shares a border with Edwards Air Force Base. These zip codes may have a larger percentage of inexperienced drivers. Areas of the state which are different from the statewide average for a mandatory factor will end up with legitimate differences in zip code losses which can only be accounted for by territory. Thus, the proposed regulations will force drivers in some parts of the state to subsidize the rates for drivers in other parts of the state.

Response to Comment:

While the commentator does not reference the report that he is referring to, it appears that the Commentator is referring to a report entitled: "Auto Insurance in California:

Differentials in Industry wide Pure Premiums and Company Territory Relativities between Adjacent Zip codes" authored by Max Tang. The findings in this report are not the motivation for the proposed regulations. The proposed regulations are intended to implement Proposition 103's requirement that the mandatory factors be given greater weight than the optional factors when calculating a consumer's insurance rate. To the extent that the commentator believes that the differences between adjacent zip codes can only be accounted for by territory, this belief does not alter Insurance Code section 1861.02 and the requirement that the mandatory factors must bear more importance on an insurer's rate. Moreover, the Commissioner disagrees with the commentator's assumption that differences in adjacent zip code pairs are due to differences in loss costs between those zip codes. The Commissioner's disagreement is reflected in the Response to Common Comments 1.1 and 1.3.

Summary of Comment (Page 10):

The commentator disagrees with the Commissioner's statement in the Policy Statement Overview and Effect of Proposed Action to the effect that Proposition 103 requires rates and premiums to be based primarily upon driving safety record, annual miles driven and years of driving experience.. Because Insurance Code section 1861.02 does not include the words "rather" and "primarily", the commentator concludes that the Commissioner's statement is misleading.

Response to Comment:
For the reasons stated in Response to Common Comments 1.1 and 1.8, the Commissioner disagrees with the commentator's remarks. While the Commissioner does not believe his statements are misleading, the Commissioner has revised the Notice of Proposed Action to clear up any confusion about what the Commissioner believes is required by Proposition 103.

Summary of Comment (Page 10):
The commentator disagrees with the comments in the rulemaking file which suggest that the proposed regulations will not impose any mandate upon local agencies or school districts. By raising the cost of automobile insurance, unions will soon attempt to negotiate higher allowances for employees that use their personal automobiles for agency business.

Response to Comment:
The Commissioner disagrees with the commentator's interpretation of Government Code sections 17500-17630. More importantly, the Commissioner disagrees with the commentator's suggestion that the proposed regulations will "rais[e] the cost of auto insurance." Because the proposed regulations result in rates which are revenue neutral, the Commissioner does not expect that the cost of auto insurance will rise. Insurers will continue to price rates competitively and rates will be based primarily upon how you drive rather than where you live. Those with better driving records and lower mileage driven will pay rates that are different from those with poor driving records or high

mileage driven. The Commissioner doubts that unions will seek to negotiate higher allowances based upon the Commissioner's proposed regulations.

Summary of Comment (Page 10-11):

The commentator disagrees with the comments in the rulemaking file which suggest that the Commissioner is not aware of any cost impacts that a representative private person or small business would necessarily incur in reasonable compliance with the proposed regulations. The commentator also disagrees with the Commissioner's assessment of the effect on small businesses and believes that statements should be removed from the assessment. The total change in premium could exceed one billion dollars. Finally, the commentator believes that the proposed regulations will force insurers to stop selling auto insurance in California and will force increased costs to employers who reimburse employees for personal use of automobiles.

Response to Comment:
The Commissioner declines the commentator's request that the Commissioner revise his assessment of the impact upon jobs, small businesses or the cost impact assessment upon private persons or businesses. Because the proposed regulations result in rates which are revenue neutral, the Commissioner does not expect that the cost of auto insurance will rise. Insurers will continue to price rates competitively and rates will be based primarily upon how you drive rather than where you live. The inclusion within the proposed regulations of an implementation plan will give insurers time to adjust their class plans and avoid unnecessary premium disruption to individual policyholders. The effect of the proposed regulations will differ substantially, depending upon the characteristics of each individual insurer. Those with better driving records and lower mileage driven will pay rates that are different from those with poor driving records or high mileage driven. The cost impacts described by the commentator are neither direct nor expected to be significant for any individual who actively shops for insurance.

Summary of Comment (Page 11):
The commentator believes there are at least ten other ways to weigh rating factors than the manner reflected in the proposed regulations. The commentator also contends that there are many different ways to reduce the effect of territory on premiums which would not require the changes proposed by the regulations.

Response to Comment:
The commentator misses the point of the proposed regulations. The fact that there may be more than one way to implement the statute is irrelevant. The Commissioner, within the sound exercise of his discretion, is charged with selecting a method for weighing the rating factors that he believes is the most appropriate.

The proposed regulations are not simply intended to reduce the effect of territory on premiums. The purpose of the proposed regulations is to properly implement Proposition 103. the proposed regulations will not only ensure that territory does not weigh more than the mandatory factors, as required by Insurance Code section 1861.02, the

regulations will also prevent any other optional factor from weighing more. For the reasons set forth in Response to Common Comment 1.1, the Commissioner believes there are no other alternatives which would be as effective in carrying out the requirements of Proposition 103.

Volume 12, Tab No. 6:

Commentator: Shawna Ackerman, on behalf of State Farm Mutual Auto. Ins. Co.
Date of Comment: March 6, 2006
Type of Comment: Written

Summary of Comment (page 1 & Exhibit 1): These pages provide introductory information about the commentator.

Response to Comment: Because these pages are not specifically directed at the agency's proposed action or to the procedures followed by the agency in proposing or adopting the Action, no response is necessary here.

Summary of Comment (page 2-3): Insurance Code sections 1861.02 and 1861.05 support the concept that auto rates must be cost based in order to comply with law. Section 1861.02 provides that optional factors adopted by the Commissioner must be substantially related to the risk of loss. Section 1861.02 also links rates that are not substantially related to the risk of loss with unfair discrimination. Section 1861.05 states that rates shall not be approved if they are excessive, inadequate or unfairly discriminatory. While Birny Birnbaum has defined "cost based" as unattainable or not required by statute, Mr. Birnbaum's definition is not necessary because the term is defined by sections 1861.02 and 1861.05.

Response to Comment:
To the extent that the commentator's remarks are directed at Mr. Birnbaum's comments, the remarks are irrelevant because they are not specifically directed at the proposed regulations or procedures followed by the Department in proposing the regulations. To the extent that the comments contend that rates must be cost based under the proposed regulations, please see the Commissioner's Response to Common Comment 1.1.

Summary of Comment (page 3-4): Although Mr. Birnbaum contends that sequential analysis does not yield cost-based or actuarially sound rates, the commentator disagrees. While multivariate techniques were not widely used when the sequential analysis was initially developed, sequential analysis was accepted as an improvement over a univariate analysis. Moreover, whether one uses a multivariate analysis or an alternative technique to determine classification relativities has nothing to do with whether or not pumping or tempering of rating factors that run through a sequential analysis is acceptable. Pumping and tempering of rating factor relativities will result in rates that are not cost based, excessive for some, and inadequate for others. Actuarial Standard of Practice no. 12 dictates that material differences in costs for risk characteristics must be appropriately reflected in the rate in order for the rates to be equitable or fair. There are significant

differences in the cost of insurance, based on location. The use of pumping or tempering will result in an arbitrary rate. In fact, the very term "weight" is arbitrary and has been given many different definitions over the last 10 years.

Response to Comment:
See Response to Common Comment 1.1.
See Response to Common Comment 1.3
See Response to Common Comment 1.7

Additional Comments: As Mr. Downer stated in his comments regarding this rulemaking proceeding, "[s]equential analysis…seeks to recognize and eliminate predictive correlation that may exist between various class factors – i.e., reducing double counting." (See comments of Robert Downer, Vol. 6, Tab 4, page 8, lns. 21-22.) The Commissioner agrees that this is the purpose of the sequential analysis method and has preserved the method for use with the proposed regulations.

To the extent that the commentator is suggesting that a multivariate approach is a better approach, the Department's Sequential Analysis Guidelines demonstrate the loss residual and the prior relativities approach that comply with Section 2632.7. The paper also states that "While we are not aware of other methods that meet the requirements of the regulations, if compliance can be demonstrated, another method could be used for performing the sequential analysis." The Department is open to other methods for a sequential analysis but it is incumbent on insurers to bring those methods to the Department's attention and to demonstrate that they comply with the requirements in Section 2632.7.

Summary of Comment (page 4-6): Consumers Union presented a number of charts and graphs which purport to show that the existing system of regulations produce irrational rates. The charts and graphs, however, do not address whether the differences in rates across zip codes are a result of differences in cost and risk. Studies conducted by the Department demonstrate that the differences in rates from different locations are based on differences in cost. Rating categories are discrete, rather than continuous, which is why consumers often see substantial changes in rates based upon zip code boundaries or mileage categories, etc. Part of the reason for the substantial difference in rates across zip code boundaries is the fact that insurers are limited in the number of frequency and severity bands that they may use to classify risks. The proposed regulations do not address territorial differentials at the zip code boundaries.

Response to Comment:
While the Commissioner does not believe it would be appropriate to eliminate the zip code rating bands, the Commissioner does agree that the number of bands should be increased in order to minimize the amount of disparity between rates for adjoining zip codes. Thus, while the existing regulations permit up to 100 zip code groupings (10 frequency bands x 10 severity bands), the Commissioner has revised the regulations so that insurers may utilize up to 400 zip code groupings (20 frequency bands x 20 severity

bands). This change is reflected in 10 California Code of Regulations section 2632.5(d) (15) & (16) of the revised draft of the proposed regulations.

Additionally, the Commissioner agrees with Consumer's Union that the disparity of rates between zip code boundaries cannot be fully explained by differences in the cost of providing insurance in those zip codes. For the reasons set forth in Response to Common Comments 1.1 and 1.3, the Commissioner recognizes that the existing regulations do not always result in rates that are cost based and that the differences across zip code boundaries do not always closely follow the patterns of the industry wide pure premium data, strongly suggesting that other non-cost based considerations are at work in many insurers' rates under the existing regulations.

Summary of Comment (page 6-7): While it is true that no one as yet can say what the exact impact of the proposed regulations will be on any particular insured, it is clear that pumping and tempering of rates will result in arbitrary rates. If an insurer were to pump the weight of the mandatory factors and leave the optional factors such as territory alone, the result would have no effect on the impact or weight of territory. Thus, the same charts and graphs used by Consumer's Union could be created to show the same rate disparity under the proposed regulations.

Response to Comment:

For the reasons explained in Response to Common Comment 1.1, both the existing regulations and the proposed regulations may result in rates that are substantially related to the risk of loss, despite the fact that both approaches permit the use of pumping and tempering in order to arrive at an auto insurance rate. The Commissioner has also revised the proposed regulations in order to increase the number of frequency and severity bands that an insurer may use, which will help to minimize the rate disparity observed in the charts and graphs presented by Consumer's Union.

Summary of Comment (page 7-9 & Exhibits 2-3): In order to ensure that a rating factor such as driving safety record is assigned as much weight as that factor bears to the risk of loss, it is important to permit insurers to use as many categories of relativities as they can to distribute the exposure among various risks within that factor. Insurers should be permitted to use driver characteristics such as those reflected in the DMV report entitled "An Inventory of California Driver Accident Risk Factors." Factors in the report such as traffic violator school dismissals, use of longer periods of time to count prior traffic incidents, use of the total number of accidents over a person's lifetime and other factors would enhance an insurers ability to increase the weight of driving safety record. To the extent that there are "masked" clean drivers, meaning drivers with citations that do not show up on their DMV record, those masked drivers result in the cost differentials being picked up by the frequency and severity bands for that driver's location. While a driving characteristic within an insured's control is not a better predictor of risk than a factor that is not in the driver's control, a difference in the expected cost for the factor is a valid criterion. The Department can assist insurers in

obtaining accurate driving safety record information and this will alleviate the need to arbitrarily pump driving safety record.

Response to Comment:
While it may be possible to develop methods for enhancing an insurers' ability to verify driving safety record, or other rating factors, such proposals are beyond the scope of this rulemaking proceeding.

Moreover, to the extent that this comment could be perceived as an objection to state laws which permit a policyholder to have tickets expunged from his/her record through traffic school, the objections are misplaced. The Legislature alone has the power to determine the circumstances under which public policy should permit a driver to have a citation expunged. Such concerns are best placed before the Legislature – not the Commissioner.

Whether an insurer obtains independent support for a policyholder's accident history verification is primarily a business decision. To the extent that an insurer would like to enhance the accuracy of its assessment of driving safety record for its policyholders, the insurer has the option to avail itself of resources such as a CLUE database or similar accident tracking system.

Additionally, as this comment alludes to, many insurers in California employ a superior good driver discount to reflect drivers that have experience that is even better than that which qualifies a driver for the good driver discount. Thus, for example, although the good driver discount looks at a person's driving record over a three-year period, some companies provide a greater discount to persons who have a clean driving record with no accidents or tickets over a five or six year period. Thus, there are extant methods that an insurer may use to strengthen the driving safety record factor which would avoid unnecessary pumping of that rating factor.

Commentator: Russina Sgoureva, on behalf of Progressive West Ins. Co.
Date of Comment: March 6, 2006
Type of Comment: Written

Summary of Comment (page 1): The proposed regulations will force companies to take a significant departure from cost-based pricing and will cause unfair subsidization of bad drivers by good drivers. The proposed regulations will be arbitrary and will not be substantially related to the risk of loss. Finally, the proposed regulations will conflict with the provisions of Insurance Code section 1861.02 and the Court's decision in *Spanish Speaking Citizens' Foundation v. Low* (2000) 85 Cal.App.4th 1179.

Response to Comment:

See Response to Common Comment 1.1.
See Response to Common Comment 1.3
See Response to Common Comment 1.8

Summary of Comment (Page 1-2):

If the proposed regulations are adopted, insurers will need to be able to assign a higher weight to the mandatory factor of annual miles driven. The Department does not permit insurers to require objective evidence of historical miles driven as part of the process for arriving at an estimated mileage figure for a particular driver. If annual mileage driven is given greater significance under the proposed regulations, policyholders will have greater incentive to underreport mileage. Therefore, the Department should allow insurers to base a policyholder's actual driving experience for the previous 12 months as the basis for rating annual mileage under a new policy. Alternatively, if projections of future mileage are going to be allowed, insurers should be given greater flexibility to impose reasonable procedures to ensure that information provided by insureds is accurate. This flexibility should include the right to verify the actual mileage driven during the previous 12 months. Insurers should also be permitted to use other methods for verification, such as verifying the place of employment, inspecting odometer readings, use of electronic vehicle data recorders, and electronic mileage tracking devices.

Response to Comment:

With respect to the suggestion for better methods to verify mileage, while it may be possible to develop methods for enhancing an insurers' ability to verify annual mileage or other rating factors, such proposals are beyond the scope of this rulemaking proceeding.

Summary of Comment (Page 2):
Insurers should be given greater flexibility to combine any mandatory factors with optional or other mandatory factors so long as the insurer can demonstrate that the proposed combination is substantially related to the risk of loss.

Response to Comment:
The Commissioner respectfully declines this proposal. In fact, the Commissioner intends to make it clear that combinations of rating factors will be limited. When an insurer combines years of driving experience with a rating factor such as gender or marital status, the Commissioner expects that the weights of those factors, taken individually, will comply with the weight ordering requirements of the regulations. The Commissioner has revised 10 California Code of Regulations section 2632.5(e) of the proposed regulations to make this clear.

Summary of Comment (Page 2-3):
The Commissioner should limit the application of the proposed regulations to the bodily injury and property damage coverages. In fact, the Mercer data only analyzed the effect of the proposed regulations on bodily injury and property damage coverage. The proposed regulations should not be extended to apply to other coverages until further

study is completed regarding the consequences of applying the proposed regulations to such coverages.

Response to Comment:
Insurance Code section 1861.02(a) provides that "automobile insurance policy" has the meaning described in Insurance Code section 660(a). Section 660(a) provides that a "policy" means an automobile liability policy, automobile physical damage, or automobile collision policy, or any combination thereof…" Section 660(c) defines physical damage coverage as including "loss or damage to an automobile insured … except loss or damage resulting from collision or upset." Insurance Code section 11580.07 defines comprehensive coverage as "coverage for loss or damage…resulting from a cause other than collision or upset." Thus, the plain reading of the statutes requires that every coverage must comply with the weight ordering requirements of Proposition 103. Based upon the plain meaning of this provision, therefore, the Commissioner disagrees with the commentator's suggestion that 1861.02(a) should only apply to property damage and bodily injury coverages.

The Commissioner believes that the effect of the proposed regulations upon the bodily injury and property damage coverages will be substantially similar to the effect the proposed regulations will have on other coverages. To the extent that comprehensive coverage bears less of a relationship to the mandatory factors of driving safety record, mileage driven and years of driving experience, the Commissioner has revised the regulations to account for the unique concerns raised by comprehensive coverage. The revision to title 10 California Code of Regulations section 2632.8(a) permits an insurer to combine comprehensive coverage with collision coverage to enhance the proposed regulations' substantial relationship to the risk of loss. The regulatory change which will allow such combination will comply with Proposition 103's weight ordering requirements insofar as comprehensive coverage and collision coverage represent a policy "combination thereof" as described in section 660(a).

Commentator: Robert Hogeboom, on behalf of The Alliance of Insurance Agents and Brokers & the Western Insurance Agents Association.
Date of Comment: March 6, 2006
Type of Comment: Written

Summary of Comment (Page 1-2):
These pages provide introductory information about the commentator.

Response to Comment: Because these pages are not specifically directed at the agency's proposed action or to the procedures followed by the agency in proposing or adopting the Action, no response is necessary here.

Summary of Comment (Page 2-3):
Insurers have argued that rates will increase for most Californians under the proposed regulations. Consumers will be upset if they have to pay higher premium with no change in their driving history. Insurance agents and brokers will be left to explain the rate

increases. While in the short term, automobile insurance may be available in lower prices for urban areas, in the long term, the insurance product will become less available in those regions of the state and consequently agents and brokers will have fewer products to choose from in offering insurance to consumers. This will be bad for consumers and insurers and will also be bad for insurance agents and brokers.

Response to Comment:

Proposition 103 requires insurers to offer automobile insurance to Californians that are good drivers, as defined in Insurance Code section 1861.025. As other commentators have pointed out, roughly 90% of Californians throughout the state qualify as good drivers. By law, insurers cannot refuse to provide insurance to a good driver, irrespective of whether that driver lives in a preferred market region or elsewhere. Thus, the proposed regulations will not diminish competition or the availability of insurance products in any particular region of the state..

Summary of Comment (Page 3-4):
It has been suggested that the proposed regulations are necessary because drivers in low-income and minority communities are being charged more for insurance because of where they live. The Low-Cost Automobile program, however, is already present in many urban centers as an alternative for low-income drivers in urban areas. The proposed regulations, by comparison, will apply to both urban poor as well as urban rich. Thus, Beverly Hills residents will receive reductions in their premium which will be subsidized by persons living in non-urban regions of the state.

Response to Comment:
While the proposed regulations may have favorable effects for urban areas, this is not the primary purpose for the proposed regulations. The primary purpose of the proposed regulations is to implement Proposition 103 and Insurance Code section 1861.02 in the way that the Commissioner believes is most consistent with the intent of the voters. Specifically, the proposed regulations will ensure that driving safety record, annual miles driven and years of driving experience will be the three most important factors in a consumer's premium computation.

Summary of Comment (Page 4 & 7-10):
The proposed regulations conflict with insurance Code section 1861.02(a). The proposed regulations do not bear a substantial relationship to the risk of loss, despite the fact that the statute requires the Commissioner to only adopt optional factors that he finds have a substantial relationship to the risk of loss. Section 1861.02 not only requires the Commissioner to adopt rating factors that are substantially related to the risk of loss, but also requires the rating factors to be implemented in a way that preserves this relationship. Rates which are arbitrary are not substantially related to the risk of loss, according to the Court in *Spanish Speaking Citizens*. Because the proposed regulations will require insurers to perform significant pumping and tempering, the resulting rates will be arbitrary and in violation of Proposition 103. The testimony of Robert Downer provides further support for the fact that pumping and tempering are arbitrary.

Depending upon the mix of pumping and tempering employed by a particular insurer, policyholders' rates will change dramatically without any change in the underlying risk for those policyholders. The resulting disruption of the automobile insurance market will be random and will result in rates that could increase for some good drivers while producing rate decreases for some bad drivers.

Response to Comment:
See Response to Common Comment 1.1
See Response to Common Comment 1.2
See Response to Common Comment 1.3
See Response to Common Comment 1.8

Summary of Comment (Page 4 & 10-11):
The Court in *Spanish Speaking Citizens' Foundation v. Low* concluded that whether or not rating factor weights are appropriate will depend upon whether the rates bear a substantial relationship to the risk of loss. The relationship to the risk of loss cannot be trumped by any other single consideration, such as the law's requirement that driving record must be considered the most important factor. Proposition 103 reflects competing requirements and any interpretation of section 1861.02 must account for the extent to which they fulfill all of these requirements. The proposed regulations will result in rates which harm experienced drivers, drivers with low annual mileage and statutory good drivers. The proposed regulations do not properly balance the competing requirements of Proposition 103 and therefore fail to comply with the *Spanish Speaking Citizens* decision.

Response to Comment:
See Response to Common Comment 1.1
See Response to Common Comment 1.2
See Response to Common Comment 1.8

Additional Comment:
The commentator contends that good drivers and drivers with low annual mileage or statutory good drivers will be harmed by the proposed regulations. In fact, more of these drivers pay unjustified rates under the existing regulations than would be under the proposed regulations The Commissioner expects good drivers and drivers with low mileage will generally receive better rates under the proposed regulations. To the extent that a rare exception to this principle exists when rates are imposed by a particular insurer, that driver will likely benefit the most from shopping among competing carriers for insurance.

Summary of Comment (Page 4-5 & 10-14):
The proposed regulations unlawfully subsidize the rates of urban drivers at the expense of rural drivers. This subsidy is unfairly discriminatory and therefore in violation of Proposition 103, which was intended to ensure that good drivers would pay less for insurance than bad drivers. The Commissioner's proposed regulations appear designed to reduce rates for the urban poor. Proposition 103 was not designed to ensure that the urban poor would have access to insurance at a lesser cost. The *Spanish Speaking*

Citizens' Foundation v. Low decision suggested that subsidizing of risks may be considered unfairly discriminatory. Both the Mercer data and the studies performed by Mr. Downer show the extent to which rural drivers will be forced to subsidize urban drivers' rates. The Low Cost Auto program already exists to aid the urban poor and it is neither necessary nor appropriate for the Commissioner to use the proposed regulations for this purpose. Moreover, the *Spanish Speaking* decision equated the concept of "unfair discrimination" with rates that are not related to the risk of loss. Thus, the proposed regulations will be unfairly discriminatory within the meaning of Insurance Code section 1861.05.

Response to Comment:
See Response to Common Comment 1.1
See Response to Common Comment 1.2
See Response to Common Comment 1.3
See Response to Common Comment 1.4
See Response to Common Comment 1.6
See Response to Common Comment 1.7
See Response to Common Comment 1.8

Additional Comment:

While the proposed regulations may provide some assistance to the urban poor, the primary purpose for drafting the proposed regulations was to bring the automobile rating factors into the correct order of importance described in section 1861.02(a).

Summary of Comment (Page 5 & 14-15):

The proposed regulations are not reasonably necessary to implement Insurance Code section 1861.02. While case law requires an agency to provide substantial evidence in support of the determination that its proposed regulations are reasonably necessary, the Commissioner's statement of necessity has been expressly rejected by the Court in *Spanish Speaking Citizens' Foundation v. Low*. The Commissioner has not offered any other rationale for his proposed regulations and has not shown a need for the regulations and the regulations therefore lack evidentiary support.

Response to Comment:
See Response to Common Comment 1.1
See Response to Common Comment 1.3
See Response to Common Comment 1.8

Summary of Comment (Page 6):

The proposed regulations are invalid because they are not consistent and are in conflict with the statute and are not reasonably necessary to effectuate the purpose of the statute. Thus, the proposed regulations violate Government Code section 11342.2. The proposed

regulations are not consistent with Insurance Code sections 1861.02, 1861.05 and Proposition 103.

Response to Comment:

The proposed regulations are consistent with the Court's decision in *Spanish Speaking Citizens' Foundation v. Low*. As is explained in the Response to Common Comment 1.8, the Court acknowledged that there may be no single correct interpretation of section 1861.02 and Proposition 103. The Court also acknowledged that the existing regulations failed to ensure that driving safety record and annual mileage driven would be the most important characteristics for a policyholder's rate. The proposed regulations, by comparison, do ensure that the mandatory factors will be most important. At the same time, the proposed regulations give insurers significant discretion to pump and temper factors only as much as necessary to bring the factors into compliance, while still preserving the overall rate's substantial relationship to the risk of loss, thereby avoiding any conflict with sections 1861.02 or 1861.05. Because the proposed regulations balance all of Proposition 103's requirements, rather than some, the proposed regulations are necessary to fulfill all of the objectives set forth by law (see Response to Common Comment 1.1.)

Commentator: Rae Ann Dankovic, on behalf of Allied Property and Casualty Insurance Company
Date of Comment: March 6, 2006
Type of Comment: Written

Summary of Comment (Page 1-2):
The proposed regulations will force the commentator's company to charge premiums that are not related to the risk of loss. Under the existing regulations, the commentator's company only had to make modest tempering adjustments to rating factors in order to bring the rates into compliance. Under the proposed regulations, however, the commentator's company will have to account for the fact that its weight for the accident frequency, accident severity, driver class (which is a combination of years licensed and other factors), its airbag factor and its multi-car rating factor. This, despite the fact that the territory factor of accident frequency is the single best predictor of a driver's likelihood of filing a claim in the next year. No matter what combination of pumping and tempering of rating factors that the commentator's company chooses to use, the resulting rate will require large adjustments to the factor weights and consequently the premiums will deviate from the cost of providing insurance.

Response to Comment:

See Response to Common Comment 1.1
See Response to Common Comment 1.3

Additional Comment:

The commentator's remarks demonstrate some of the contradictions in the existing regulations. As the commentator concedes, its company engages in tempering to adjust its factors under the existing system. Thus, while the commentator states that rates must be substantially related to the risk of loss, the commentator also acknowledges that it deviates its rates from the risk of loss under the existing system. Additionally, it is notable that rating factors such as whether a policyholder insures one or more cars is weighted more heavily under the existing regulations than the mandatory factors. There is absolutely no reason to believe that whether a policyholder insures one vehicle or two vehicles is a more important characteristic for risk than that driver's safety record, annual miles driven, or years of driving experience. Yet, under the existing regulations, insurers are permitted to weigh such optional factors more heavily than the mandatory factors. The proposed regulations, on the other hand, will prevent such abuse of the optional rating factors and bring rating factor weights into the order of compliance required by Proposition 103.

Summary of Comment (Page 3 & Attachments A and B):
The commentator has presented a demonstration of the effect of purely tempering the optional factors in order to comply with the proposed regulations. This approach is consistent with the approach taken by Instruction Set 3 from the Mercer data and the Downer study conducted in 2003. The resulting rates produce rate increases for policyholders with the below average incidence of bodily injury claims and a rate decrease for policyholders who have the highest incidence of bodily injury claims.

Response to Comment:
The Commissioner has previously rejected a pure tempering approach as producing rates which are the least reasonable method for compliance with the proposed regulations. For the reasons stated in Response to Common Comment 1.3 and 1.6, this approach is not a reasonable estimation of how insurers will comply with the proposed regulations.

Summary of Comment (Pages 3-5 & Attachments C, D and E):
The commentator has presented a demonstration of the effect of pumping and tempering rating factors in combination in order to comply with the proposed regulations. The resulting rates reduce the rate disruption due to tempering of the optional factors but create rate disruptions for the pumped mandatory factors. Thus, the rates for inexperienced drivers and senior citizens are increased, while the rates for other drivers decrease slightly. In addition to the effect of pumping years of driving experience, the rate changes caused by tempering territory interact with a driver's rates as well. Thus, some elderly drivers will see rate decreases (if they live in a high risk territory) while other elderly drivers in low risk territories will see rate increases (due to the combination of the increase in the years of driving experience factor and reduction in territory's influence on a rate). These changes do not have any correlation to whether elderly drivers are more or less risky than they were under the existing regulatory system. The rate changes which must be performed, therefore, are arbitrary.

Response to Comment:

The pumping and tempering required by the proposed regulations is no more arbitrary than the pumping and tempering that the commentator acknowledges it engages in to comply with the existing regulations. The difference between the approaches, however, is that the pumping and tempering under the proposed regulations will further a greater social good – that of returning driving safety record, annual miles driven and years of driving experience into the proper order. The pumping and tempering required under the existing regulations, on the other hand, does not further this goal. As the California Farm Bureau's study demonstrates (see Response to Common Comment 1.1), the pumping and tempering which would be required by the proposed regulations will not cause substantial deviation from cost based pricing and will result in rates which bear a correlation to the risk of loss that is close to that observed under the existing regulations.

Summary of Comment (Page 6 & Attachment F):
While the Department has made public statements which suggest that the proposed regulations may be implemented without the need for premium increases in rural areas, this does not seem possible to the commentator. The commentator cannot absorb the premium undercharges and will be forced to substantially increase rates for large groups of drivers in order to offset the decreases for other drivers. Moreover, because class plans are designed to be revenue neutral, it would not make sense for an insurer to offset rate decreases for some insureds without creating rate increases for other insureds.

Response to Comment:
The comments referenced by the commentator reflect the Commissioner's recognition that insurers are currently obtaining a substantial profit in the private passenger automobile insurance business under the existing regulations. As some commentators have noted, insurers have experienced substantial profit that could be used to impose a reduction in the base rates for policyholders state wide which would result in the proposed regulations imposing very little impact upon a given policyholder's premium.

Summary of Comment (Page 6):
The proposed regulations will not comply with Insurance Code section 1861.05 because the rates will be excessive for some policyholders and inadequate for other policyholders. Moreover, the Court in *Spanish Speaking Citizens' Foundation v. Low* held that section 1861.02 must be interpreted in light of section 1861.05. The Court also stated that rates which are arbitrary would violate section 1861.02 and the prohibition against rates which are not substantially related to the risk of loss. Because the proposed regulations will result in rates which are not substantially related to the risk of loss, the rates will violate section 1861.02. The rates under the proposed regulations deviate from cost based pricing and therefore are not substantially related to the risk of loss.

Response to Comment:

See Response to Common Comment 1.1
See Response to Common Comment 1.3
See Response to Common Comment 1.8

Summary of Comment (Page 7):
The top 5 insurer groups have almost 50% of the California auto insurance market share. The commentator's insurer holds approximately 1% of the California auto insurance market share. Smaller companies, like the commentator's company, will be burdened significantly by the proposed regulations and were not considered as part of the Mercer data. Although larger insurers may be able to balance the cross-subsidies required by the proposed regulations, smaller insurers cannot. The effect of over and under pricing insurance risks in various regions of the state will cause more under priced risks to be sold over time, rather than over priced risks and rates will consequently have to be increased. Niche insurers will lose rural policyholders and will force the insurer to seek additional rate increases for rural drivers to make up for the lost rural policyholders. Over time, smaller insurers will be forced to cease actively writing automobile insurance coverage. This will increase the concentration of market share among the larger insurers.

Response to Comment:
The threat of under pricing risks exists under the existing regulations just as it will under the proposed regulations. Until insurers actively work to give the mandatory rating factors the weight that Proposition 103 requires, one cannot speculate as to whether insurance risks will be "under priced." By requiring insurers to give driving safety record and annual mileage more weight, insurers will also be forced to give greater focus to the correlation to loss costs for these factors. The result will be to avoid under pricing and will ensure that insurers give greater consideration to rating factors that are equally reflective of the risk of loss, but which have been ignored because of the instinctive desire of insures to fall back on territory as the most important rating characteristic. The Commissioner does not expect smaller insurers to stop writing private passenger auto insurance.

Summary of Comment (Page 8):

Automobile insurance will become less affordable in rural areas and the availability of insurance in urban areas will shrink. Thus, the number of uninsured motorists will grow in rural areas and insurers will be reluctant to write risks in urban areas where they cannot make up the cost of writing insurance in those areas.

Response to Comment:

Proposition 103 requires insurers to offer automobile insurance to Californians that are good drivers, as defined in Insurance Code section 1861.025. As other commentators have pointed out, roughly 90% of Californians throughout the state qualify as good drivers. By law, insurers cannot refuse to provide insurance to a good driver, irrespective of whether that driver lives in a preferred market region or elsewhere. There is no evidence to suggest that the proposed regulations will diminish competition.

To the extent that the commentator believes that the proposed regulations will cause more drivers to drive uninsured, it appears that the commentator's suggestion is merely

speculative at this point. The Commissioner, in fact, anticipates that less drivers will be uninsured in the future, due to the increased availability of automobile insurance required by the good driver requirements of Proposition 103 and the expansion of the Low Cost Automobile program which has increased the availability of affordable insurance for persons who cannot afford it.

Commentator: Sam Sorich, on behalf of the Association of California Insurance Companies
Date of Comment: March 6, 2006
Type of Comment: Written

Summary of Comment (Page 1-2):
If the proposed regulations are adopted, they should be implemented over a period of no less than four years to ensure flexibility to determine individual implementation schedules and to avoid a one-size-fits-all approach to implementation. There should be no prescribed method or caps to the amount of rate change allowed during a policy period.

Insurers should be given sufficient time to develop, test and file class plans. A July 1, 2006 filing date for new class plans, therefore would be unreasonable and impractical. If the Department intends to require immediate class plan filings upon approval of the regulations, the Department should give insurers flexibility to avoid unanticipated negative impacts. To this end, the Department should freely permit amended filings throughout the implementation period.

Finally, because the proposed regulations will force insurers to assign significant weight to annual miles driven as a rating factor, the Department must give insurers the authority to verify a policyholders' mileage. While no single verification method should be mandated, insurers should be given the ability to confirm mileage in the manner deemed effective, efficient and supportable.

Response to Comment:

The Commissioner does not intend to require rates to be filed by July 1, 2006. The Commissioner has taken similar insurer input into account and has decided upon a reasonable schedule for implementation which will give insurers flexibility to decide upon the best approach for implementation, but will also ensure that compliance is achieved in a timely manner. Therefore, while the Commissioner believes that four years is too much time to implement the proposed regulations, he has revised the regulations to provide for a two-year schedule.

The Commissioner disagrees with the commentator's suggestion that there should be no prescribed caps (up or down) to the method for complying with the regulations. The Commissioner, therefore, has set a minimum threshold for compliance in the first year. This schedule provides that insurers must bring their rates at least 15% of the way towards full compliance with the proposed regulations in the first class plan filing, but

gives insurers discretion to implement the remaining 85%, so long as the implementation is completed by the two year anniversary of the date the regulations are filed with the Secretary of State. See revisions to 10 Cal. Code of Regulations, section 2632.11. The revisions to the regulations do not attempt to impose a "one-size-fits-all approach" and recognize that different insurers will feel comfortable using different methods for implementation.

With respect to the suggestion for better methods to verify mileage, while it may be possible to develop methods for enhancing an insurers' ability to verify annual mileage or other rating factors, such proposals are beyond the scope of this rulemaking proceeding.

Commentator: John Richmond, on behalf of the California State Automobile Association Inter-Insurance Bureau
Date of Comment: March 6, 2006
Type of Comment: Written

Summary of Comment (Page 1):
As the Court in *Spanish Speaking Citizens' Foundation v. Low* recognized, the existing regulations represent an inspired way to harmonize the internally inconsistent provisions of Proposition 103. The current system is not broken and should not be altered. The proposed regulations, by comparison, will only favor one objective of Proposition 103 to reduce the rate impact of territory at the expense of another objective which prohibits arbitrary rates. The proposed regulations will cause substantial premium shifting for consumers because there would have been little reason to go to all of this effort if the proposed regulations were a mere academic exercise with no effect on consumers.

Response to Comment:
See Response to Common Comment 1.1
See Response to Common Comment 1.3
See Response to Common Comment 1.8

Summary of Comment (Page 1-2):
The proposed regulations appear to require insurers to file a class plan without an accompanying rate filing because the Department traditionally has required a rate filing whenever there are changes to the base rate. This may not be possible, in the event that an insurer files a revenue neutral class plan but determines that it must adjust its base rates in order to comply with the change in the weighting of the optional factors. The proposed regulations should therefore be modified to permit insurers to forego filing a rate change so long as the class plan is revenue neutral.

Response to Comment:
Contrary to the commentator's suggestion, the Commissioner does intend to require a class plan and rate filing for purposes of compliance with the proposed regulations. A class plan and rate filing will be required irrespective of whether the company intends to make adjustments to its base rate. The Commissioner has revised the proposed regulations to make this clear. See revisions to 10 California Code of Regulations section

2632.11(c). The purpose of this change will be to preserve the Commissioner's ability to ensure that the rates submitted in compliance with the proposed regulations are neither excessive nor inadequate.

Summary of Comment (Page 2):
Under the existing regulations, the Department essentially requires insurers to permit self-certification of annual miles driven. Because the proposed regulations will require insurers to give annual miles greater weight in the future, this increases the risks attendant to self-rating. The proposed regulations, therefore, should permit insurers to independently verify annual mileage in order to avoid arbitrary rates.

Response to Comment:

The commentator mischaracterizes the current method for verifying annual miles driven. The Department disagrees that, under existing regulations, the Department essentially requires self-certification of annual mileage. However, to address comments such as these, the Department has issued a Notice of Proposed Action to adopt proposed mileage verification regulations. That proposal is not part of this rulemaking proceeding.

Commentator: Alice Bisno, on behalf of the Automobile Club of Southern California
Date of Comment: March 6, 2006
Type of Comment: Written

Summary of Comment (Page 1-2):
The proposed regulations present a challenge to the commentator's ability to provide coverage at a fair price to its policyholders. Reducing the importance of territory in auto insurance ratemaking is likely to result in a more arbitrary pricing system. The proposed regulations will make changes to rates without any change in the underlying costs for those rates. Therefore, the commentator submits that the proposed regulations are not in the best interest of insurance companies in the state.

Response to Comment:
See Response to Common Comment 1.1
See Response to Common Comment 1.3

Summary of Comment (Page 2):
Existing regulations limit the ability of an insurer to combine mandatory factors with other rating factors for purposes of establishing a rate. The proposed regulations should allow insurers to combine the mandatory factors of years of driving experience and driving safety record. This combination will allow insurers to vary the amount of a surcharge for a traffic citation or accident, depending upon the number of years of driving experience for that driver. Under the existing regulations, for example, insurers with less experience often must pay a greater surcharge simply because their class of drivers tends to have more accidents or citations. This change will allow fairer and more accurate pricing. The commentator has presented proposed language to implement this change.

Response to Comment:

The Commissioner respectfully declines this suggested change. Proposition 103 requires insurers to make the mandatory factors the most important factors in an auto insurance rate. The Commissioner is extremely hesitant to permit insurers to combine mandatory or optional factors because of the risk that this practice may dilute the importance of the mandatory factors and threaten the hierarchy of importance set forth by section 1861.02 and Proposition 103.

In fact, when an insurer combines years of driving experience with a rating factor such as gender or marital status, the Commissioner expects that the weights of those factors, taken individually, will comply with the weight ordering requirements of the regulations. The Commissioner has revised 10 California Code of Regulations section 2632.5(e) of the proposed regulations to make this clear.

Summary of Comment (Page 2):
The proposed regulations should clarify that pumping and tempering of rating factors is permitted. An insurer that seeks to retain cost-based pricing and avoid premium dislocation will need the ability to pump as well as temper the mandatory and optional rating factors in order to comply with the proposed regulations. Pumping and tempering, while artificial, also make compliance more feasible. The commentator has presented proposed language to implement this change.

Response to Comment:
The Commissioner's proposed regulations, like the existing regulations, were intended to permit either pumping or tempering, as necessary in order to bring the rating factors into proper alignment. In order to make this intention clearer, the proposed regulations have been revised. Specifically, the Commissioner has added section subdivision (d)(4) to section 2632.8 of title 10 of the California Code of Regulations to make this clear. While the revised language is not identical to that proposed by the commentator, the effect of the change will be the same.

Summary of Comment (Page 3):
The proposed regulations should be changed so that insurers may combine bodily injury and property damage coverages for weight testing purposes. Some insurers, such as the commentator's insurer, consider each coverage separately for pricing and weighting. This proposed change will allow insurers to combine the coverage without engaging in burdensome and costly reprogramming. The commentator has presented proposed language to implement this change.

Response to Comment:
The Commissioner agrees with this proposed change and has revised the regulations accordingly. Specifically, the Commissioner has revised section 2632.8(a) of title 10 of the California Code of Regulations to make this clear. While the revised language is not identical to that proposed by the commentator, the effect of the change will be the same.

Summary of Comment (Page 3):
The proposed regulations should be changed so that insurers may combine collision and comprehensive coverages for weight testing purposes. The substantial majority of the commentator's policyholders purchase both collision and comprehensive coverage. Weight testing comprehensive coverage by itself is highly problematic and results in a rate that bears no relationship to the mandatory factors. Thus, the resulting rate is less cost based and does not bear a substantial relationship to the risk of loss. Because the mandatory factors do have a relationship to the risk of loss for collision coverage, combining the two coverages for rating purposes will increase the relationship to the risk of loss and minimize the premium shifting among insureds. The commentator has presented proposed language to implement this change.

Response to Comment:
The Commissioner agrees with this proposed change and has revised the regulations accordingly. Specifically, the Commissioner has revised section 2632.8(a) of title 10 of the California Code of Regulations to make this clear. While the revised language is not identical to that proposed by the commentator, the effect of the change will be the same. See also Response to Common Comment 1.9.

Summary of Comment (Page 3-4):
The proposed regulations should increase the number of frequency and severity zones from ten to fifteen zones. This will help insurers to enhance pricing and allow for rates that are more reflective of the actual exposure, could create smaller rate differentials between territories and will reduce premium dislocation in rural areas. The commentator has presented proposed language to implement this change.

Response to Comment:
The Commissioner agrees that the number of bands should be increased in order to minimize the amount of disparity between rates for adjoining zip codes. Thus, while the existing regulations permit up to 100 zip code groupings (10 frequency bands x 10 severity bands), the Commissioner has revised the regulations so that insurers may utilize up to 400 zip code groupings (20 frequency bands x 20 severity bands). This change is reflected in 10 California Code of Regulations section 2632.5(d) (15) & (16) of the revised draft of the proposed regulations. The revision, of course, gives even greater flexibility to insurers to establish rating bands than the revision proposed by the commentator.

Summary of Comment (Page 4-5):
The proposed regulations should be phased in over a three-year period. In order to avoid some insurers from obtaining an unfair advantage over other insurers who implement the regulations in good faith, the proposed regulations should establish clear and measurable compliance standards. The commentator has presented proposed language to implement this change. The proposed language would require a minimum of 33% compliance in each year over the three-year period, but would also permit an insurer to implement the changes more rapidly if they choose to do so.

Response to Comment:
The Commissioner agrees, in principle, with the commentator's suggestion. The Commissioner has taken similar insurer input into account and has decided upon a reasonable schedule for implementation which will give insurers flexibility to decide upon the best approach for implementation, but will also ensure that compliance is achieved in a timely manner. Therefore, while the Commissioner believes that three years is too much time to implement the proposed regulations, he has revised the regulations to provide for a two-year schedule. This schedule also provides that insurers must bring their rates at least 15% of the way towards full compliance with the proposed regulations in the first class plan filing, but gives insurers discretion to implement the remaining 85% in the manner each insurer sees fit, so long as the implementation is completed by the two-year anniversary of the date the regulations are filed with the Secretary of State. The Commissioner agrees with many of the suggestions of the commentator concerning the need for clear and measurable compliance standards, and the revisions to the regulations reflect those proposals. See revisions to 10 Cal. Code of Regulations section 2632.11.